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TREASURY FOR DOHNER, POGGI

E.O. 12958: N/A

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SUBJECT: JAPAN MARKET VIEW: WORST TWO DAY DROP IN 17 YEARS

¶1. (U) In its worst two-day drop in 17 years, Japan's benchmark Nikkei 225 Stock Average dropped 5.6 percent on Tuesday, January 22. The broader Topix index fell 5.7 percent, as Japanese markets mirrored Asian markets, downward trajectory. The Nikkei's 9.3 percent fall over the last two days of trading removes 39.2 trillion yen (\$369 billion) in value from the Tokyo Stock Exchange.

¶2. (U) In the midst of global financial market turmoil, Tokyo's financial sector remains relatively healthy, as Mizuho Financial Group's recent \$1.2 billion investment in Merrill Lynch suggests. On the heels of non-performing loan crises during the 1990s, major Japanese banks do not appear to have significant direct exposure to the same sub-prime investment risks that are plaguing their American and European counterparts. Major Japanese banks have taken write-offs to the existing sub-prime investments they hold, however the amounts are relatively small compared to their annual profits and capital base.

¶3. (U) In addition, the January 29 scheduled \$5 billion stock swap buyout of Nikko Cordial Corp. by Citigroup Inc. is still on track, despite Citi's own recent spate of sub-prime troubles. The swap ratio will be calculated based on the three day average price of Citigroup, Inc. stock from January 15-17 of \$26.35. Since this represents a 37% drop in Citigroup's stock price from this fall when the deal was reached, Nikko Cordial shareholders will now receive more Citigroup stock for each share of Nikko Cordial that they own.  
SCHIEFFER